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No. 81-2120

In the

Supreme Court of the United States

October Term, 1981

Durham Industries, Inc.,

Petitioner,

—against—

The North River Insurance Company,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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The Questions Presented

1. Can the obligor of a surety bond fraudulently misuse the procedures of the United States Court system, to delay payment of a justified claim without incurring civil tort liability to the party wronged?

2. Is perjury, in answers to interrogatories, which is part of a scheme to delay payment of a justified claim under a surety bond, conduct of such a degree of moral turpitude and of such wanton dishonesty as to imply a criminal indifference to civil obligations and thereby form the basis of an award of punitive damages?

3. Was there sufficient evidence to support the jury's verdict in favor of the petitioner, awarding compensatory damages based upon prima facie tort, resulting from the respondent's misuse of Federal Court procedures?

4. Were the fraudulent actions of the respondent insurance company, sufficient to constitute such a bad faith breach of its surety bond; as would provide the basis for the imposition of punitive damages?

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—against—

THE NORTH RIVER INSURANCE COMPANY,

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Petitioner prays that a writ of certiorari issue to review the Order of the United States Court of Appeals for the Second Circuit entered on the 25th day of February, 1982.

The opinion of the United States Court of Appeals is printed in Appendix "A" hereto and is not yet officially reported.

Jurisdiction

This is an action brought to recover both compensatory and punitive damages against the respondent insurance company, arising out of the respondent's improper and fraudulent misuse of the process of the United States District Court for the Southern District of New York, in order to delay payment of the petitioner's justified claim under a surety bond, while it attempted to recover its collateral, which it had negligently allowed to lapse; from a person

other than the petitioner. The petitioner alleges that the respondent was able, by the use of false allegations of fact in its answer to the Complaint and perjury in answers to interrogatories to continue to assert a spurious defense, in the United States District Court for the Southern District of New York, for a period of two (2) years. This delay required the petitioner to borrow money in the open market to replace the amount of its justified claim which had not been paid by the respondent, thereby causing the compensatory damages alleged herein.

Statement

The circumstances leading up to this case arose out of the issuance of a Bill of Lading, covering a shipment of toys from Japan to Philadelphia, by the Ta Peng Steamship Company to Durham Industries, Inc. When the shipment covered by the Bill of Lading failed to arrive on the designated ship, Durham commenced an action against Ta Pen seeking recovery of the amount paid to the shipper under its letter of credit in Japan. This action was assigned to Judge Charles E. Stewart, Jr., in the United States District Court, Southern District of New York (Index No. 73 Civ. 4740).

Durham obtained an attachment of a bank account of the steamship company, containing approximately $300,000.00. The steamship company then purchased a Surety Bond, which supported the issuance of an Order discharging the attachment of its bank account. The Surety Bond was issued by the respondent herein, North River Insurance Co., and guaranteed payment of any judgment which might be recovered against Ta Peng. The insurance company received a letter of credit in the amount of $300,000.00, from Ta Peng which was to act as collateral for the issuance of the Surety Bond, and was drawn on

Franklin National Bank and replaced by a letter of credit in the same amount drawn on the First National City Bank. The letter of credit had a life of one (1) year and was renewed by the steamship company for one (1) year. The North River Insurance Company allowed the letter of credit to expire after its second year without taking any steps to obtain its renewal or to make any withdrawal thereunder. Ten (10) days after the expiration of the above letter of credit on April 18, 1976, the prior action came on for trial before Judge Stewart. After trial, Judge Stewart entered judgment, in the amount of $223,670.08, in favor of the plaintiff, Durham, against the defendant in the former action, Ta Peng. Ta Peng did not pay the said judgment. The bond issued by North River Insurance Company contained an obligation that North River Insurance Company would pay to the plaintiff in the former action, Durham Industries, Inc., the amount of any judgment which might be recovered in that action against Ta Peng Steamship Co., Ltd. Durham then turned to North River Insurance Company for payment. Upon refusal of the insurance company to make payment of the judgment which had been recovered against Ta Peng Steamship Co., Ltd., an action was commenced by Durham Industries, Inc., against North River Insurance Company seeking recovery under the terms of the Surety Bond. This action was commenced on June 13, 1976, in the United States District Court, for the Southern District of New York and bore Index No. 76 Civ. 2433 (Judge Lasker). The North River Insurance Company interposed an answer to the complaint, including the affirmative defense of fraud and collusion between Durham and Ta Peng, which it alleged, released it from its obligation under the terms of the bond.

On or about June 13, 1976, North River Insurance Company commenced its own action against Ta Peng Steam-

ship Co., in the New York Supreme Court, seeking to compel Ta Peng to reinstate the collateral for the bond. On August 25, 1976, this action between North River Insurance Company and Ta Peng Steamship Co., Ltd., was settled in accordance with a written confession of judgment in which Ta Peng Steamship Co., Ltd., agreed to make twelve (12) monthly payments of $20,000.00 each, to North River Insurance Company. The North River Insurance Company received three (3) such payments.

The North River Insurance Company, in order to hide this settlement and its receipt of the above funds under the settlement of its action against Ta Peng Steamship Co., Ltd., then proceeded to give false answers to the plaintiff's interrogatories under oath.

The petitioner contends that the affirmative defense of fraud interposed by the respondent, North River Insurance Company contained several patent falsehoods, which were asserted as statements of fact, with the sole intention of misleading Judge Lasker into thinking that there was some factual basis for the affirmative defense of fraud. As a result of this assertion, defendant was able to continue this defense for two (2) years in an attempt to delay paying the plaintiff's justified claim, until such time as it had recouped its collateral.

All of the judges who have examined the record in this case agree that the respondent insurance company misused the process of the United States District Court in order to delay the day upon which it would be required to pay the petitioner's justified claim, until it had an opportunity to recover its lapsed collateral. Judge Sweet in the United States District Court, for the Southern District of New York, the Trial Judge in this case, on March 25, 1981, made the following statement on the record:

"I have spent some time also considering if there is any other theory upon which Punitive Damages might be appropriate, and it has occurred to me that under the evidence submitted, it may well be that there was a fraud on the Court committed by virtue of the false answers to interrogatories. The difficulty I have with that theory is that even if that be so, I don't see how that fraud is the cause of any special damages. It seems to me that those answers, the fraudulent answers, that is, that there had been no communications between Ta Peng and North River when in fact there had been such communications, I don't see that those answers, the falsity of those answers, were the cause of any injury to the Plaintiff. Therefore, even if the pleadings were amended again to conform to the proof to state a claim of fraud on the Court, I don't see any causation which would arrive at any special damages which in turn could give rise to Punitive Damages."

On March 26, 1981, Judge Sweet again referred to this matter on the record, in the following language:

"With respect to the case which you have cited to me, the Court of Appeals case, Doralee Estates against City Service, the underlying violation there committed by the Defendant upon which the Punitive Damages were granted, was a violation of the prior Stipulation, and I suppose as I understand it, we are in a somewhat anomalous position where you can get Punitive Damages on any cause in New York, providing you meet the requirements to show malice, etc., except perhaps Prima Facie Tort, but that is my understanding of the law.

This gives me particular trouble in this case for the simple reason that I think the conduct of the insur-

ance company in this matter was indeed outrageous. There is no question about it. I indicated on the record yesterday, if I could figure out a way to deal with fraud on the Court, I certainly would do it, but I can't, and I am a little bit frustrated by the state of the New York law."

The dissenting opinion in the United States Court of Appeals for the Second Circuit in this case, considered this matter in the following language:

"The jury was entitled to find that North River delayed, by the assertion of its unfounded affirmative defense of fraud, the payment of its legal obligation to Durham. As an excuse for this behavior, North River asserts that it desired to attempt to recover the $223,670.08 from a third party before it paid that amount to Durham. This surely is not a proper justification for North River's action. Conduct such as this results in no gain to the public whatsoever. Indeed, the public is the victim of such shoddy and dishonest business dealings.

If conduct such as that by North River is to be considered proper, then some shrewd persons may attempt to avoid timely payment of their debts, ostensibly while waiting to collect their accounts receivable. If the stakes are high enough, they may even be willing to defend a lawsuit to delay payment, knowing that what they can earn on the money at market rates will more than cover their attorney's fees and the artificially low legal rate of interest they will eventually have to pay on the judgment entered against them. Under the rationale of today's majority's opinion, they will be able to engage in such dishonest behavior, secure in the knowledge that they

will prevail should their creditors sue them upon a claim of prima facie tort.

In short, in my view Durham clearly has established all the elements of a case of prima facie tort. It sustained obvious injury—the loss of the use of $223,670.08—as a result of North River's deliberate action in asserting the unfounded fraud defense. The assertion of this defense, ordinarily a lawful action, was rendered tortious by North River's lack of any legitimate, legally cognizable excuse for asserting it. New York law provides Durham with a remedy for such injury."

The majority opinion in the Court of Appeals, in essence, agreed with the above evaluation of the insurance company's conduct in the following language:

"The most the jury permissibly could infer from the proof was that North River asserted the affirmative defense of fraud in order to postpone the day it would have to make good on its bond, without any expectation of prevailing on the merits of the defense. The jury might have concluded that North River falsely answered plaintiff's interrogatories to conceal the existence of its lawsuit against Ta Peng, but such concealment resulted from the same motivation. The evidence established beyond peradventure that North River acted purely out of self-interest to mitigate or avoid a business loss. It was insufficient to support liability on a theory of prima facie tort."

The majority opinion in the United States District Court absolves the respondent insurance company from liability for damages, despite its improper conduct herein, because it was seeking to recapture collateral which it had negligently allowed to lapse.

It is respectfully submitted, that the majority opinion in the United States Court of Appeals for the Second Circuit, is in direct contradiction to the law of the State of New York, as set forth in the case of *Gordon* v. *Nationwide Mutual Insurance Co.*, 30 N.Y.2d 427, 437 (1972), cert. denied, 410 U.S. 931 (1973); and *Walker* v. *Sheldon*, 10 N.Y.2d 401, 405 (1961); *Borkowski* v. *Borkowski*, 39 N.Y.2d 982 (1976).

Reasons for Granting the Writ

This petition raises substantial and important questions concerning the power of the United States Courts to award damages, both compensatory and punitive, to an innocent party who has been injured by the fraudulent misuse of its process. It is an ancient maxim that the law abhors damage without remedy. Furthermore, there is a conflict between the law as set forth in the decisions of the New York State Court of Appeals and the majority opinion of the United States Court of Appeals for the Second Circuit, which requires reconciliation by this Court.

CONCLUSION

The petition for certiorari should be granted.

Respectfully submitted,

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